

The Federal Crop Insurance Program: Opportunities and Challenges

Barry J. Barnett

University of Georgia

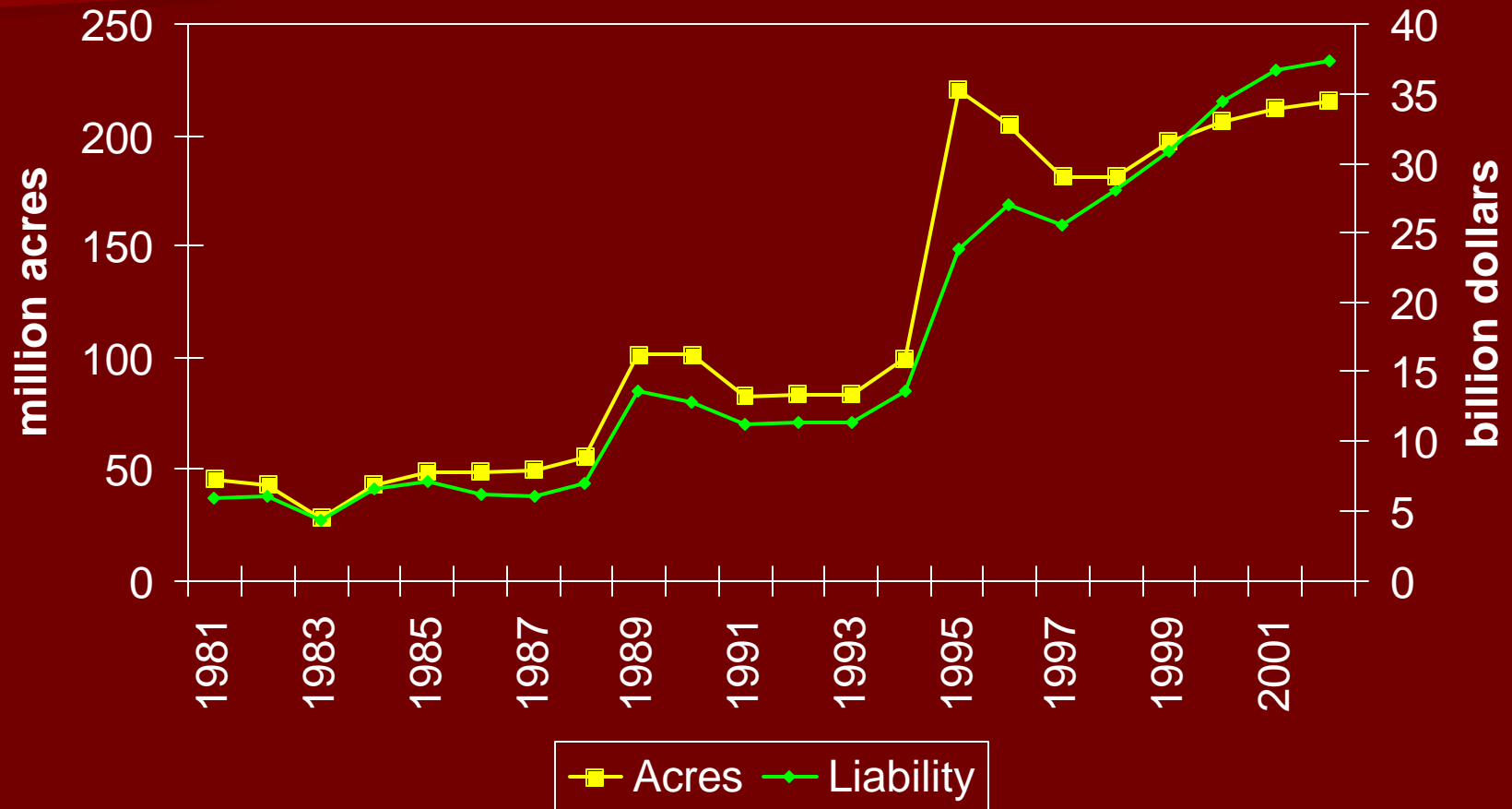
Federal Crop Insurance Program

- Administered and regulated by RMA.
- Provides federally subsidized insurance products to agricultural producers.
- Public-private partnership between the federal government and private insurance companies.
- Federal Crop Insurance Board, appointed by the Secretary, is responsible for approving all new risk management products and expansion of existing products.

Outline

- Environment.
 - Expansion.
 - Multiple Program Objectives.
 - Multiple Stakeholders.
 - Complexity.
- Challenges and Opportunities.
- Important Considerations.

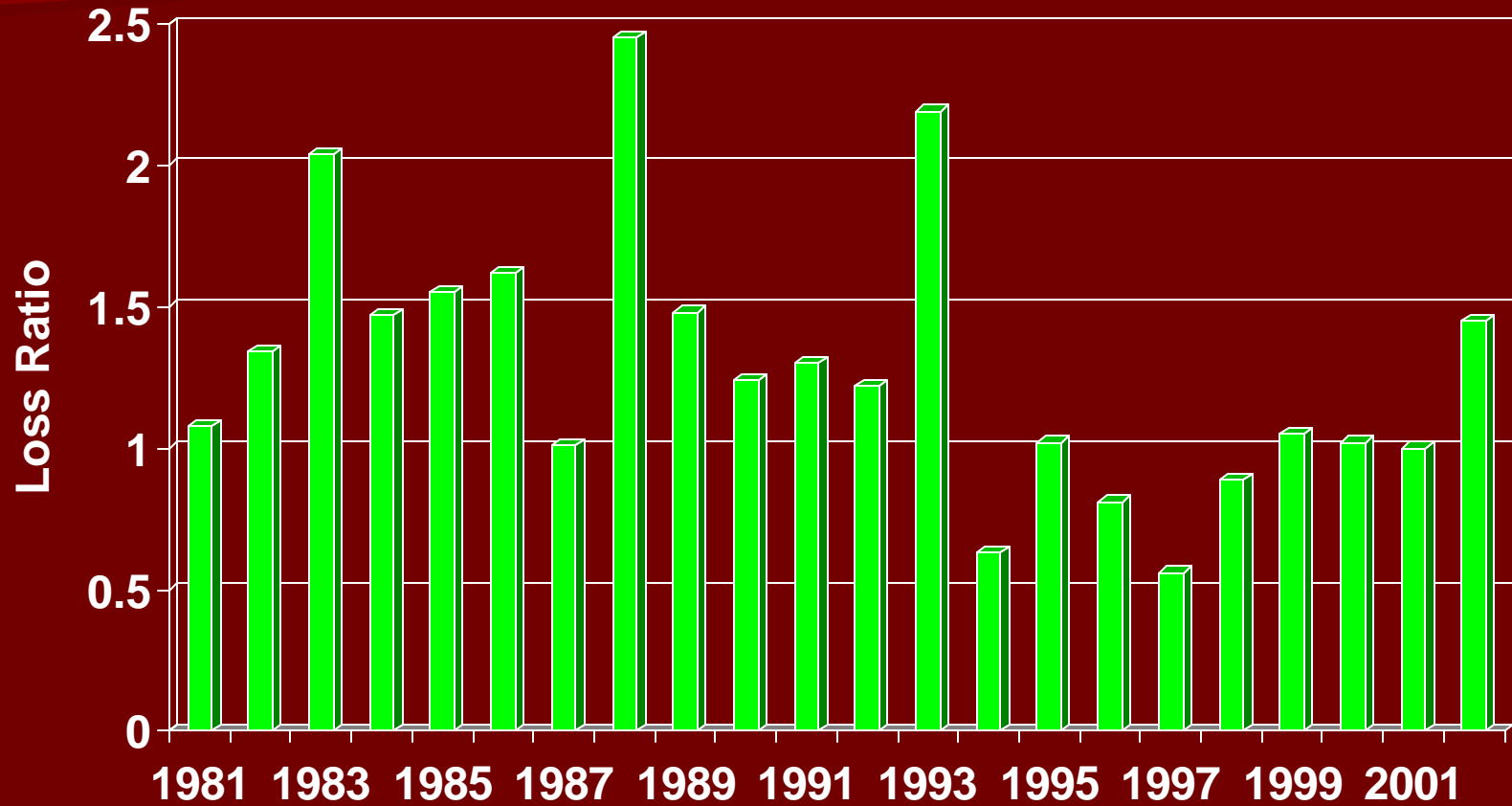
Expansion



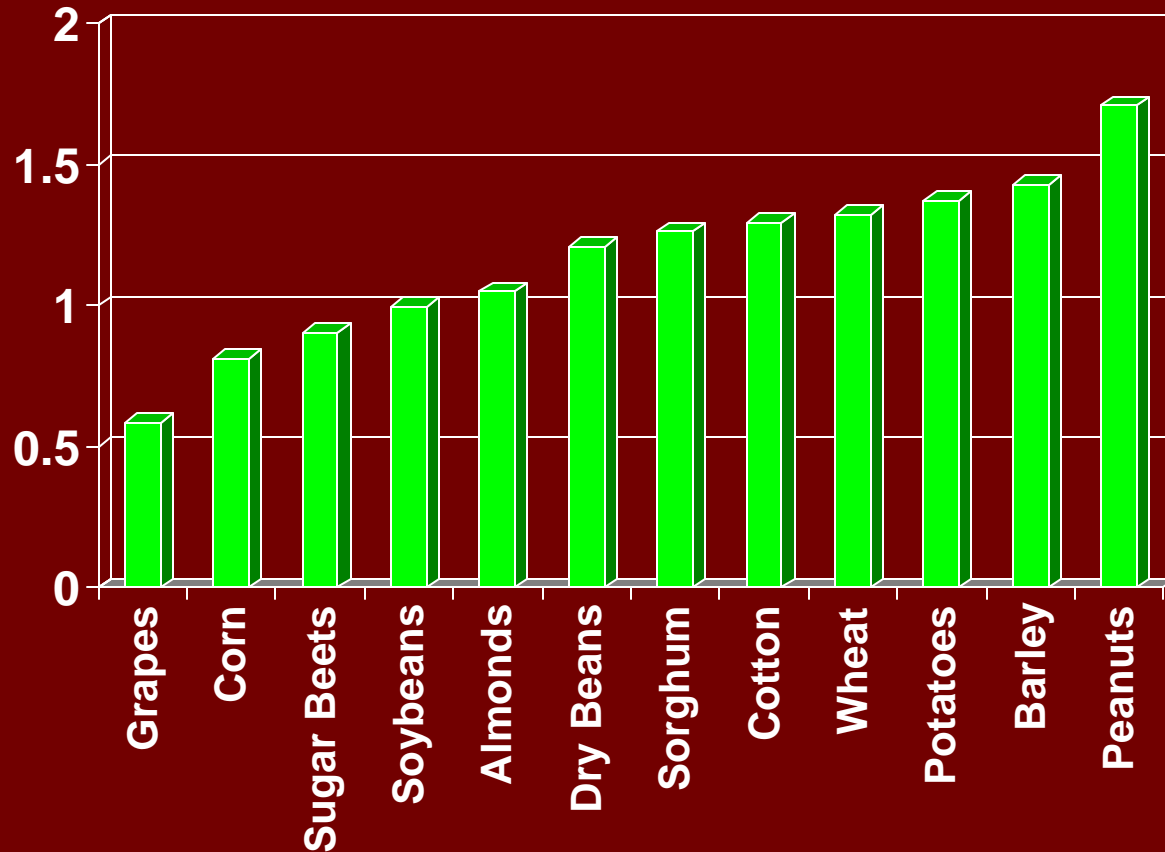
Multiple Program Objectives

- Reduce demands for disaster assistance.
 - Increase participation.
 - Premium subsidies.
 - SRA provisions.
 - Expand into new commodities.
 - Expand into new regions.
- Actuarial soundness.
- Are these compatible?

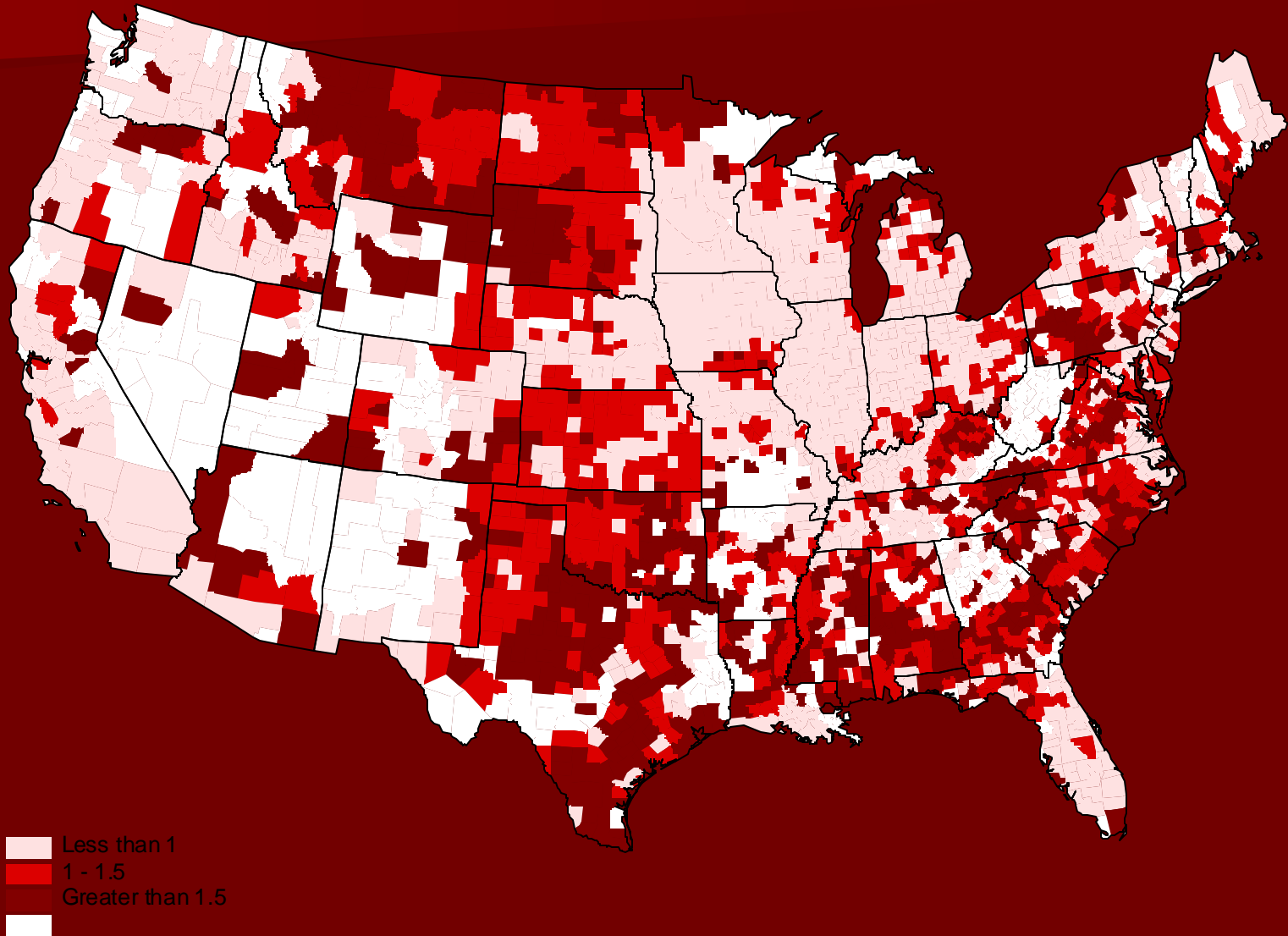
Loss Ratios



Loss Ratios, by Crop, 1981-1999



Loss Ratios, 1981-2002



Multiple Stakeholders

- Crop and livestock farmers.
- Lenders.
- Private insurance companies.
- Retail insurance agents.
- RMA employees.
- Private reinsurance companies.
- Taxpayers.

Complexity

- Insurance is inherently complex.
 - Underwriting: risk assessment and classification.
 - Actuarial: establishing premium rates for each risk classification.
 - Loss adjustment: calculating indemnities.
 - Compliance: investigate fraud and abuse.
- Contrast to other USDA farm programs.

Complexity

- Agricultural insurance is even more complex.
 - Risk varies by commodity.
 - Risk varies by region.
 - Risk varies by producer.
 - More frequent claims than other insurance lines.
 - Difficult to monitor farmer behavior.
 - Losses are often spatially-correlated.

Complexity

- Scope compounds complexity.
 - 1981: approx. 5,000 county-commodity-product combinations.
 - 2002: more than 38,000 county-commodity-product combinations.
 - Authority for livestock products.
 - 508h submission process.

Challenges and Opportunities

- How much expansion is desirable?
 - How many commodities?
 - How many products for each commodity?
 - Should similarity to existing products be a factor when considering new product submissions?

Challenges and Opportunities

- Maintaining core products.
 - Expansion stretches limited RMA budget.
 - Over 70% of premium in 2002 was for farm-level yield and revenue insurance on corn, soybeans, cotton, and wheat.

Challenges and Opportunities

■ Delivery system.

- Internet sales with premium discounts.
- Some agencies are specializing in only a few products.
- Some companies are reluctant to take loss risk on new products.

Important Considerations

- Not all risks are insurable.
 - Must be able to assess and classify risk.
 - Must be able to accurately estimate frequency and severity.
 - Must be able to determine when a loss has occurred and the severity of the loss.
 - Must be able to verify that the loss was accidental and unintentional.
 - If not, high loss ratios.

Important Considerations

- Not all farmers want (or need) insurance.
 - Many ways to manage risk.
 - Farmers consider entire portfolio of farm and off-farm activities.
 - Limit to participation rates!
 - Other federal farm programs reduce price risk. This increases the subsidies required to encourage crop insurance purchasing.

Important Considerations

- Crowding out.
 - Large-scale expansion into new commodities and new products may crowd-out private sector initiatives. Can't compete against highly subsidized crop insurance.

Important Considerations

- Things change.
 - Need to continually reassess appropriate federal role in providing agricultural insurance.

Summary

- Environment.
 - Expansion.
 - Multiple Program Objectives.
 - Multiple Stakeholders.
 - Complexity.
- Challenges and Opportunities.
- Important Considerations.